TRANSCRIPT OF RECORD

SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1940

No. 393

THE UNITED STATES, PETITIONER

vs.

ARTHUR PELZER

ON WRIT OF CERTIORARI TO THE COURT OF CLAIMS

PETITION FOR CERTIORARI FILED SEPTEMBER 3, 1940
CERTIORARI GRANTED OCTOBER 21, 1940

BLANK PAGE

SUPREME COURT OF THE UNITED STATES

October Term, 1940

No. 393

THE UNITED STATES, PETITIONER

vs.

ARTHUR PELZER

ON PETITION FOR A WRIT OF CERTIORARI TO THE COURT OF CLAIMS

INDEX

259228—40——1

BLANK PAGE

1 In United States Court of Claims

No. 43923

ARTHUR PELZER, PLAINTIFF

vs.

THE UNITED STATES OF AMERICA, DEFENDANT

I. Petition

Filed April 29, 1938

Comes now the plaintiff, Arthur Pelzer, by his attorney, Robert A. Littleton, and respectfully shows to the Court:

1. That plaintiff is a citizen and resident of the United States and resides at Montgomery, in the State of Alabama.

2. On the 14th day of July 1932, the plaintiff created an irrevocable trust for the benefit of his eight grandchildren then living, viz: Weldon W. Doe, Jr., Alice Pelzer Webber, Camilla Webber, Amelia K. Webber, Arthur Pelzer Webber, Elizabeth Joseph, Alice Joseph, and W. F. Joseph, Jr. In creating said trust the plaintiff
2 deposited with the trustee named property of the value of $49,998.83.

3. In paragraph 2 of said trust instrument it is provided that for a period of ten years from and after the date of July 14, 1932, the net income from the corpus of the trust be accumulated and invested and reinvested from time to time by the trustee; and that after the expiration of ten years the trustee is required to distribute the net income from the trust to each of the trustor's grandchildren named above who may then be living and be twenty-one years of age or over in proportion to the number of grandchildren then living, whether born before or after the date of July 14, 1932.

4. It is provided in said trust instrument that in the event of the death of any of the beneficiaries specifically named in said instrument, without leaving issue, then, and in that event, the interest of the deceased beneficiary in the trust property shall belong to his surviving brothers or sisters, if any, and if none, then to the other grandchildren of the trustor per stirpes, subject to the terms of the trust.

5. The period of the trust is for twenty-one years after the death of the last survivor of all of the trustor's grandchildren who are living at the date of July 14, 1932, whose names are set forth in the trust instrument, at which time the trust shall cease and determine, and the corpus of the trust, with any accumulation, shall then be
3 distributed to the grandchildren of the trustor, born after the date of July 14, 1932, and who may at that time be living (each such living grandchild to receive a grandchild's equal share), and the issue of all deceased grandchildren to receive the deceased parent's share of the trust property per stirpes.

6. Section 504 (b) of the Revenue Act of 1932 provides as follows: "In the case of gifts (other than of future interests in property) made to any person by the donor during the calendar year, the first $5,000 of such gifts to such person shall not, for the purposes of subsection (a), be included in the total amount of gifts made during such year."

7. In making a return of the gifts evidenced by the trust instrument of July 14, 1932, to the eight grandchildren of the donor therein named, the plaintiff omitted to claim an exclusion of $5,000 for each of the named beneficiaries; but did claim a specific exemption of $50,000 which left no net value of said gifts subject to tax.

8. Plaintiff avers that in reporting the 1932 gifts, as aforesaid, for tax purposes, he is entitled to eight $5,000 exclusions in the aggregate amount of $40,000, and that inasmuch as only $9,998.83 of the specific exemption of $50,000 allowable is absorbed by the 1932 gifts the balance of such specific exemption of $40,001.17 is allowable in a subsequent year or years.

9. Plaintiff avers that during the calendar year 1933 he made
4 further gifts to the beneficiaries named in said trust instrument in the aggregate amount of $29,800 together with three additional gifts of $6,000 each to the following named persons, viz: Francis P. Doe, Elizabeth K. Webber, and Alice E. Joseph. That the gifts of 1933 amounted to the aggregate of $47,800.00, of which only $3,000 is the net amount subject to tax, which is absorbed by the specific exemption of $40,001.17 carried over from the year 1932. Plaintiff is not liable for a gift tax for the year 1933.

10. Plaintiff avers that during the year 1934 he made gifts in the aggregate amount of $38,803.00 to the persons named in the trust instrument of July 14, 1932; gifts in the aggregate amount of $153,060.00, in trust for the following named beneficiaries, viz: Eva L. Pelzer, Francis P. Doe, Elizabeth K. Webber, and Alice E. Joseph, and gifts in the amount of $6,000 each to the following named persons, viz: Francis P. Doe, Elizabeth K. Webber, and Alice Joseph. That no part of the 1934 gifts, in the aggregate amount of $38,803.00, is subject to tax because of the eight $5,000 exclusions allowable. That from the 1934 gifts in the aggregate amount of $153,060.00, four $5,000 exclusions are allowable, which leaves $133,060.00 of such gifts subject to tax; and from the gifts in the aggregate amount of $18,000, three $5,000 exclusions are allowable, which leaves $3,000 of such gifts subject to tax. For the year 1934 there was $37,001.17 of the specific exemption of $50,000 unused by gifts in prior years, and after
5 the same is allowed from the 1934 gifts in the aggregate amount of $138,060.00 after exclusions, the net amount of such gifts subject to tax is $101,058.83.

11. Plaintiff avers that during the year 1935 he made gifts in the aggregate amount of $39,531.25 to the persons named in the trust instrument of July 14, 1932, under which he is entitled to eight exclu-

sions in the amount of $5,000 each, which leaves no part of said gifts subject to tax.

12. Plaintiff avers that the total net gifts during the years 1932, 1933, 1934, and 1935 upon which a gift tax is due is the aggregate amount of $101,058.83; whereas, the Commissioner of Internal Revenue has erroneously computed the net amount of said gifts subject to tax to be $242,193.08, and assessed and collected a tax thereon in the aggregate amount of $16,681.70. The correct amount of the tax for which plaintiff is liable on the net value of said gifts for all years is the sum of $3,693.82; but through error there has been collected from plaintiff by the Treasury Department of defendant the aggregate amount of $16,681.70 together with interest in the amount of $465.45.

13. On November 25, 1935, plaintiff paid a tax of $533.96 and accrued interest of $53.54 computed by the Bureau of Internal Revenue on net value of gifts for the year 1933. On the return of the net value of gifts for the year 1934, plaintiff computed and paid in March 1935, a tax of $4,538.82 and thereafter the Bureau of Internal Rev-
6 enue determined an additional tax of $6,865.17 on the net value of the gifts for 1934, which plaintiff paid on March 14, 1936, together with accrued interest in the amount of $411.91. On the return of the net value of the gifts for the year 1935, the plaintiff paid a total of $4,743.75 on March 15, 1936.

14. On July 27, 1937, the plaintiff filed claims for the refund of $587.50 tax and interest paid for the year 1933; of $7,277.08 tax and interest paid for the year 1934; and of $4,743.74 tax and interest paid for the year 1935.

15. On or about January 17, 1938, the Commissioner of Internal Revenue acted upon said claims and allowed the claim for the year 1933 in the amount of $270.07, and rejected same in the amount of $317.43; allowed the claim for the year 1934 in the amount of $1,011.25, and rejected it in the amount of $10,804.65, and allowed the claim for the year 1935 in the amount of $600 and rejected it in the amount of $4,143.75.

16. Plaintiff avers that he is not liable for a gift tax for the years 1932, 1933, and 1935, and the amount of the gift tax due and payable for the year 1934 is the amount of $3,693.82. That there has been erroneously and illegally collected from the plaintiff for the years 1933, 1934, and 1935 a gift tax and interest in the aggregate amount of $13,453.33, for which he prays judgment of this Court, together with interest from the dates of payment as aforesaid, less refunds heretofore made.

7 17. Plaintiff avers that he has at all times borne true allegiance to the United States; that he is the true and lawful owner of the claim sued upon, that the same has not been assigned, that there are no offsets or counterclaims thereto, that said claim is due and owing to the plaintiff; and that no claim therefor has been made except as stated above.

Wherefore, plaintiff sues the defendant for the amount of $12,453.30, less refunds heretofore made, together with interest thereon from the dates of payment above stated, for which amount judgment is prayed.

ROBERT A. LITTLETON,
Attorney for Plaintiff,
1021 Tower Building, Washington, D. C.

[*Duly sworn to by Arthur Pelzer; jurat omitted in printing.*]

9 *II. General traverse*

Filed June 7, 1938

And now comes the Attorney General, on behalf of the United States, and answering the petition of the claimant herein, denies each and every allegation therein contained; and asks judgment that the petition be dismissed.

JAMES W. MORRIS,
Assistant Attorney General.

III. Argument and submission of case

On January 10, 1940, this case was argued and submitted on merits by Mr. Robert A. Littleton for plaintiff, and by Mrs. Elizabeth B. Davis for defendant. Littleton, J., did not participate.

IV. Special findings of fact, conclusions of law, and opinion of the court by Williams, J.

Filed March 4, 1940

10 Mr. Robert A. Littleton for the plaintiff.

Mrs. Elizabeth B. Davis, with whom was Mr. Assistant Attorney General Samuel O. Clark, Jr., for the defendant. Mr. Robert N. Anderson was on the brief.

The court, upon the stipulation of facts and the evidence, makes the following

SPECIAL FINDINGS OF FACT

1. The plaintiff, Arthur Pelzer, is a citizen of the United States and a resident of Montgomery, Alabama.

2. On July 14, 1932, the plaintiff executed a trust instrument, which is hereinafter referred to as the "children's trust." This instrument, after reciting that the trustor (the plaintiff) was transferring certain personal property to the trustee in trust for the use and benefit of the trustor's living grandchildren (eight in number, being specifically named) and other grandchild and/or grandchildren of the trustor as might hereafter be born during the life of the trust, provided: first, the trustee was to manage the property, to sell and to invest and

reinvest the proceeds from sales with the provision that he should consult with the trustor about investments and changes in and disposition of the trust property, it being distinctly agreed, however, that by this it is not intended, nor shall it be construed to be intended, that the Trustor shall have any right to change any of the terms of
11 this instrument, or distribution of the trust estate, nor any
right to revoke or change any provisions hereof, nor be entitled to receive any economic, financial, or other benefit from the trust estate." It is further provided that the trustee shall collect the income and pay expenses and distribute the net income in the manner thereinafter stated.

Paragraphs 2, 3, and 4 (Exhibit A) of the trust instrument are as follows:

"2. For a period of ten years from date hereof the net income from this trust estate shall by the Trustee be accumulated and invested and reinvested from time to time. At the expiration of said ten years the Trustee shall thereafter pay in semiannual, quarterly, or monthly installments (whichever is more practicable) an equal grandchild's distributive share of the net income from this estate to each of the Trustor's now living grandchildren whose names are set out above, who may be then living and be twenty-one years of age or over, said payments to continue to each during his and/or her respective life; and as and when each of Trustor's remaining grandchildren who are now living, and whose names are hereinabove set out, respectively reaches the age of twenty-one years, the Trustee shall thereafter pay in said semiannual, quarterly, or monthly installments to him and/or her for and during his and/or her respective life an equal grandchild's distributive share of the net income from the trust estate; but, in the meantime, and during the respective minority of the remaining of the hereinabove specifically named now living grandchildren, all net income not required to be paid out under the terms hereof to adult grandchildren and to or for grandchildren hereafter born, shall be invested and reinvested according to the terms of this instrument to the end that the net trust income may be accumulated during the period authorized by law.

"Should the Trustor have other grandchildren born hereafter during the life of this trust, then each and all of said hereafter born grandchildren shall be entitled to participate in the trust estate equally with the other grandchildren hereinabove named, and to receive an equal grandchild's distributive share as herein provided, except as to distributions of net income that may have been made prior to the birth of such hereafter born grandchild or grandchildren; provided, however, and except further that for ten years from the date hereof, the net income from this estate shall be accumulated and in-
12 vested and reinvested as hereinabove provided, and subject
further to the terms of this trust. At the expiration of ten years from date, then as to any and all of Trustor's grandchildren who may be hereafter born and then living, the Trustee shall thereafter

during the life of this trust pay in said periodical installments to or for each of said now unborn, but hereafter born grandchildren if then living, an equal grandchild's distributive share of the net income from this trust estate. Such payment of net income shall be made direct to each after born grandchild when and after he or she reaches twenty-one years of age, and during the minority of such after born grandchild may be paid out or expended directly by the Trustee for the support, maintenance, comfort, and education of such grandchild, or be paid by the Trustee to the mother thereof for said purposes.

"3. Should any of the grandchildren of Trustor die during the life of this trust without leaving issue, then said deceased grandchild's distributive share of the net income hereunder shall belong to his and/or surviving brother and/or sister, if any, and if none, then to the other grandchildren per stirpes, subject to the terms of this trust; but should any of the grandchildren of Trustor die leaving issue, then said issue shall be entitled to receive the deceased grandchild's share of the income per stirpes, subject to the terms of this trust. During the life of this trust, all net income payable by the Trustee to or for the issue of a deceased grandchild shall be paid by the Trustee to or for him at the time and in the manner hereinabove at the end of the preceding paragraph provided in the case of a grandchild.

"4. This trust shall continue, and the income therefrom be distributed as hereinabove provided, until twenty-one years after the death of the last survivor of all of Trustor's grandchildren who are now living, and whose names are set forth hereinabove, at which time it shall cease and determine, and the corpus, with any accumulation, shall then be distributed free from this trust among such, if any, of Trustor's grandchildren born hereafter who may at that time be living (each such living grandchild to receive a grandchild's equal share), and the issue of all deceased grandchildren, the issue of a diseased grandchild, to receive the deceased parent's share per stirpes."

The remaining provisions of the trust instrument deal with the substitution of a trustee if the trustee named resigned or died, the giving of bond by the trustee, etc., which provisions are not material to a decision of this case.

13 3. On March 15, 1933, the plaintiff filed a gift tax return for the year 1932, showing total gifts for that year in the amount of $50,000 on account of transfers made by the plaintiff to the trustee of the children's trust during that year and claiming a specific exemption of $50,000, resulting in no net gifts and no gift tax for the year 1932. In an audit of this return the Commissioner of Internal Revenue determined the total gifts for 1932 to be $49,998.83 and allowed a specific exemption in a like amount, resulting in no net gifts and no gift tax for that year. Plaintiff was notified of this audit on January 18, 1935.

4. On March 15, 1934, plaintiff filed a gift tax return for the year 1933, showing total gifts in the amount of $18,000 representing three gifts of $6,000 each to plaintiff's daughters, Frances P. Doe, Elizabeth

K. Webber, and Alice E. Joseph, from which was deducted three exclusions of $5,000 each, resulting in gross gifts for that year of $3,000 from which was deducted a specific exemption of $3,000, resulting in no net gifts and no tax due for that year.

When the Commissioner of Internal Revenue audited plaintiff's gift tax return for the year 1933 he determined that the total gifts made by plaintiff for the year 1933 amounted in the aggregate to $47,800, and that in addition to the three gifts of $6,000 each to Frances P. Doe, Elizabeth K. Webber, and Alice E. Joseph, reported in said return, the amount of $29,800 transferred to the trustee of the children's trust should be included in the 1933 gifts. The Commissioner, in said audit for 1933, allowed three exclusions of $5,000 each; and computed gross gifts by plaintiff for 1933 in the amount of $32,800 from which he allowed a specific exemption of $1.17, being the unused portion of the specific exemption of $50,000 carried over from the year 1932.

As a result of the foregoing changes made in the plaintiff's gift tax return for the year 1933, the Commissioner determined a gift tax liability against plaintiff for the year 1933 in the amount of $533.96, plus interest thereon in the amount of $53.54, which tax and interest was paid by plaintiff on November 27, 1935.

5. On December 28, 1934, the plaintiff executed a trust instrument, hereinafter referred to as the "adult trust." This agreement,
14 after reciting that it was an irrevocable trust indenture between the plaintiff as trustor and the trustee by which the trustor transferred certain personal property to the trustee in trust for the use and benefit of the Trustor's wife and daughters (Eva L. Pelzer, his wife, Frances P. Doe, Elizabeth K. Webber, and Alice E. Joseph, his daughters), provided: first, that the trustees should manage the property and should have the right to change or sell and to invest and reinvest the proceeds from the sale but should confer with the trustor about investments and changes in and disposition of the trust property, "it being distinctly agreed between the parties, however, that by this it is not intended, nor shall it be construed to be intended, that the Trustor shall have any right to change any of the terms of this instrument or distribution of the trust estate, nor any right to revoke or change any provision hereof, nor be entitled to receive any economic, financial, or other benefit from the trust estate."

Paragraphs 3 and 4 (Exhibit B), of the trust instrument are as follows:

"3. The net income from said trust estate shall be paid to the said beneficiaries, Eva L. Pelzer, Frances P. Doe, Elizabeth K. Webber, and Alice E. Joseph, share and share alike, in quarterly installments, adjustments to be made from time to time according to the earnings of the trusts.

"Upon the death of Trustor's wife, her share of the income shall be divided equally among all of Trustor's grandchildren; and upon the death of any of Trustor's daughters, her share of the income shall

go to her children in equal shares. In the event of the death of any grandchild leaving issue, such grandchild's share hereunder shall go to such issue, and if no issue, to such grandchild's heirs at law. Any payment required hereunder to be made to a grandchild, or issue of a grandchild, who may be under twenty-one years of age may be paid by the Trustee to the parent of such grandchild, if living, for his or her benefit until arrival at age twenty-one; and if the parent of such grandchild is not living, any payment required hereunder may be disbursed by the Trustee in its discretion for the benefit of such grandchild until arrival at age twenty-one; and paid direct thereafter.

"4. Said Trust shall continue throughout the lives of the several beneficiaries hereinabove named, and upon the death of any, the share of said deceased beneficiary shall continue in trust for the chil-
15 dren or grandchildren of said beneficiary, share and share alike, as set forth herein; that is, the one-fourth share of Trustor's wife shall continue in trust for all the grandchildren of the Trustor, share and share alike, and the one-fourth share of any of the daughters of said Trustor dying, shall continue for the children of said daughter, share and share alike; if any, and if none, for her heirs at law, to be finally distributed as hereinafter provided.

"Upon arrival of any of the grandchildren of Trustor at the age of twenty-two, said grandchild's grandmother being deceased, or upon her decease thereafter, this trust shall cease and determine as to that grandchild's share of the one-fourth of this trust held for the benefit of Trustor's wife; and said share shall be paid over to said grandchild free of this trust, to the end that upon the arrival of the youngest of Trustor's grandchildren at the age of twenty-two years, said Trustor's wife being deceased, this trust shall cease and determine as to said one-fourth; and similarly, upon arrival of any of the grandchildren of Trustor at the age of twenty-two years, said grandchild's mother being deceased, or upon her decease thereafter, this trust shall cease and determine as to that grandchild's share of the one-fourth of this trust held for the benefit of his or her mother (which shall be an equal share with the other issue of his or her mother); and said share shall be paid over to said grandchild free of this trust, to the end that upon the arrival of the youngest of the issue of the deceased daughter of Trustor at the age of twenty-two years, this trust shall cease and determine as to such deceased daughter's one-fourth. In the event of the death of a daughter leaving no issue, her share hereunder shall go to her heirs at law."

The remaining provisions of the trust deal with the various rights of the trustee, the giving of bond and the substitution of trustee, which provisions are not material to a decision of this case.

6. On March 15, 1935, the plaintiff filed a gift tax return for the year 1934 showing total gifts in the amount of $209,863. Of this amount, $153,060 was paid to the trustee of the "adult trust," $6,000 to each of the trustor's daughters, Frances P. Doe, Elizabeth K. Webber, and Alice E. Joseph, and $38,803 to the trustee of the "chil-

dren's trust." On this return plaintiff claims specific exclusions of $58,803 and a specific exemption of $37,001.17, resulting in total net gifts of $114,053.83 and a tax of $4,538.82.

16 On March 14, 1936, plaintiff filed an amended gift tax return for the year 1[illegible] showing total gifts in the amount of $209,863 (the same as shown on the original return) from which was deducted specific exclusions in the amount of $20,000, leaving net gifts for the year of $189,863, resulting in a tax due of $11,403.99. Inasmuch as a tax of $4,538.82 was paid on the original return, this amended return showed an additional tax of $6,865.17, which amount, together with interest of $411.91, was paid on March 14, 1936. The Commissioner in an audit of this return accepted this amended return as filed by the plaintiff as correct.

7. On March 14, 1936, plaintiff filed a gift-tax return for the year 1935 showing the total amount of $39,531.25 paid to the trustee of the "children's trust" and claimed no exclusions and no specific exemption. This resulted in a tax due of $4,743.75, which was paid on that same date. The Commissioner of Internal Revenue in an audit of this return accepted the return as filed by the plaintiff as correct.

8. On July 27, 1937, plaintiff filed a claim for refund of gift tax for the year 1933 in the amount of $587.50. This claim for refund was based on the contention that the gift-tax return for 1932 was incorrect and that plaintiff was entitled to eight specific exclusions of $5,000 each for that year, since in making transfers to the children's trust the plaintiff made a gift to each of his eight living grandchildren; and further that the specific credit of $50,000 was exhausted in 1932 only to the extent of $10,000. This claim alleged further that as to the year 1933 plaintiff was also entitled to eight specific exclusions of $5,000 each, which in addition to the exclusions already allowed would result in no net gifts and no tax due for that year.

When the Commissioner of Internal Revenue acted upon plaintiff's claim for refund for the year 1933, he reopened plaintiff's gift-tax liability for the year 1932 and allowed one exclusion of $5,000 on account of the transfer to the trustee of the children's trust. This allowance resulted in the Commissioner determining gross gifts for 1932 of $44,998.83 from which a specific exemption of $50,000 was allowed, leaving no taxable gifts for that year. The Commissioner also allowed plaintiff an additional exclusion of $5,000 for the year 1933 on account of the transfer to the children's trust in the 17 amount of $29,800. The Commissioner thus allowed a total of four $5,000 exclusions for the year 1933, and by carrying over from 1932 $5,001.17 of the specific exemptions of $50,000 not used in that year, he adjusted the amount of plaintiff's net taxable gifts for 1933 to the amount of $22,798.83.

As a result of the above adjustments the Commissioner determined an overassessment for 1933 in the amount of $270.07, which amount, together with interest of $31.59, was refunded to the plaintiff on October 15, 1937. In a statement attached to the certificate of over-

assessment it is stated that the plaintiff is entitled to only one $5,000 exclusion in each of the years with respect to the property placed in trust for the grandchildren, since the gifts in so far as the children are concerned are gifts of future interest against which no exclusions are allowable.

On January 17, 1938, the plaintiff was advised that his claim for refund for 1933 was rejected as to any excess over the amount allowed.

9. On July 27, 1937, the plaintiff filed a claim for refund of gift tax for the year 1934 in the amount of $7,277.08, based upon the contention that he was entitled to eight exclusions of $5,000 each on account of the transfer to the trustee for the "children's trust" and four exclusions of $5,000 each on account of the transfer to the trustee of the "adult trust," and in addition to a specific exemption in that year of $37,001.17 not consumed in prior years.

The Commissioner of Internal Revenue in acting on the claim for refund for the year 1934 allowed one exclusion for the transfer to the trustee of the "children's trust," one exclusion for the transfer to the trustee of the "adult's trust," and three exclusions for other gifts in that year, making a total of $25,000, which was $5,000 in addition to the amount claimed and allowed on the amended return. (See Finding 6 above.) As a result of these adjustments, the Commissioner reduced the amount of gifts for preceding years from $32,798.83 to $22,798.83 and disallowed the specific exemption, inasmuch as the entire specific exemption of $50,000 had been applied to gifts in the preceding years, resulting in a total tax liability for the year 1934 of $10,449.98.

18 On October 15, 1937, the Commissioner of Internal Revenue issued a certificate of overassessment to the plaintiff showing an overassessment of $1,011.25, which, together with interest of $99.73, was refunded to plaintiff on that same date. In a statement attached to this certificate of overassessment the Commissioner stated that he was disallowing the additional exclusions claimed on account of the property placed in trust for the benefit of the grandchildren for the same reason that he had disallowed it in 1933. (See Finding 8 above.)

On January 17, 1938, the plaintiff was advised that his claim for refund of gift tax for the year 1934 was rejected as to any excess over the amount allowed.

10. On July 27, 1937, the plaintiff filed a claim for refund of gift tax for the year 1935 in the amount of $4,743.74, claiming that the plaintiff was entitled to eight specific exclusions on account of the transfers made to the trustee of the "children's trust" in that year.

The Commissioner of Internal Revenue in acting on this claim for refund allowed one exclusion of $5,000 for the transfer to the trustee of the "children's trust." As a result of adjustments for preceding years, the Commissioner reduced the amount of gifts for preceding years from $222,661.83 to $207,661.83, resulting in a total tax liability for the year 1935 of $4,143.75.

On October 15, 1937, the Commissioner of Internal Revenue issued a certificate of overassessment to the plaintiff showing an overassess-

ment of $600, which, together with interest of $58.48, was refunded to the plaintiff on the same date. In a statement attached to this certificate of overassessment the Commissioner stated that he was disallowing the claim for eight specific exclusions, giving the same reason that he had given for the year 1933.

On January 17, 1938, the Commissioner of Internal Revenue notified the plaintiff by letter that the claim for refund for 1935 was rejected as to any excess over the amount allowed.

11. True copies of the two trust agreements and the certificates of overassessment to which are attached statements of the final audits made by the Bureau of Internal Revenue for each of the years 1932, 1933, 1934, and 1935 are attached to the stipulation as Exhibits A, B, C, D, and E.

19 *Conclusion of law*

Upon the foregoing special findings of fact, which are made a part of the judgment herein, the court decides as a conclusion of law that the plaintiff is entitled to recover but entry of judgment will be withheld pending submission by the parties of a computation of the amount to be included therein.

Opinion

Williams, Judge, delivered the opinion of the court:

Plaintiff seeks to recover gift taxes alleged to have been overpaid for the years 1932, 1933, 1934, and 1935. The facts have been stipulated by the parties and are not in controversy.

The plaintiff executed a trust instrument on July 14, 1932, which is herein referred to as the "children's trust." The instrument recited that it was created for the benefit of the trustor's living grandchildren (eight in number, being specifically named) and other grandchildren that might thereafter be born during the life of the trust. The instrument further provided that for a period of 10 years from the date of its execution the income from the trust fund should be accumulated and invested, that at the expiration of such ten-year period the trustee should pay an equal grandchild's distributive share of the income to each of the grandchildren who were then living and twenty-one years of age or over, and that as each grandchild reached twenty-one years of age the trustees should pay the share of the income to him. If other grandchildren were born during the life of the trust, they were entitled to participate therein on the same basis as the living grandchildren. If any of the grandchildren died leaving issue, his share should belong to his issue, but if he should die without issue his share should go to his surviving brother and/or sister, if any, and if none, then to the other grandchildren. At the termination of the trust the corpus was to be divided between the grandchildren or their survivors.

On December 28, 1934, plaintiff executed a trust instrument, herein referred to as the "adult trust." The income of this trust was to be

paid to the trustor's wife and three daughters in equal proportions.

Upon the death of the wife, her share of the income was to be
20 divided equally among the trustor's grandchildren, and upon
the death of either of the daughters her share was to go to her children in equal shares. At the termination of the trust the corpus was to go to the grandchildren of the trustor as each of them reached the age of twenty-one years.

In each of these trusts the plaintiff retained no economic interest or legal control over the property transferred, and the trustee acquired no economic interest in the property so transferred, but is charged only with the safekeeping and management of the property transferred for the benefit of the persons named. The plaintiff was powerless to change the terms of the said instruments, regain control of the property transferred, or change the interest of the beneficiaries therein. Also, the trustee is likewise powerless, and the trust instruments are self executing..

During the years 1932, 1933, 1934, and 1935, plaintiff made gifts to the children's trust, and during the year 1934 he made a gift to the trustee of the adult trust.

Plaintiff filed gift-tax returns for the years 1932, 1933, 1934, and 1935. Claims for refund for each of the years involved were duly filed and allowed in part and disallowed in part by the Commissioner of Internal Revenue. In passing on these claims the Commissioner allowed the plaintiff one $5,000 exclusion for each of the gifts to the children's trust and one $5,000 exclusion for the gift to the trustee for the adult trust. The basis of plaintiff's claim for refund and of this suit is that the plaintiff was entitled to eight $5,000 exclusions for each of the gifts for the children's trust and to four $5,000 exclusions for the gifts to the adult trust.

The question for decision is whether the taxpayer is entitled to a $5,000 exclusion in each of the years 1932, 1933, 1934, and 1935, for each of the gifts made in trust for the benefit of eight named and living grandchildren; and for the year 1934 for each of the gifts made in trust for the benefit of the taxpayer's wife and three daughters.

The Commissioner of Internal Revenue holds that in the case of the annual gifts made in trust for each of the named living grandchildren of the taxpayer only one $5,000 exclusion is allowable for each year, and that in the case of the gifts made in 1934 in trust for the taxpayer's wife and three daughters only one $5,000 exclusion is allowable.

21 Section 501 of the Revenue Act of 1932 (47 Stat. 245) provides as follows:

"(a) For the calendar year 1932 and each calendar year thereafter a tax, computed as provided in section 502, shall be imposed upon the transfer during such calendar year by any individual, resident or nonresident, of property by gift.

"(b) The tax shall apply whether the transfer is in trust or otherwise, whether the gift is direct or indirect, and whether the property

is real or personal, tangible or intangible; but, in the case of a non-resident not a citizen of the United States, shall apply to a transfer only if the property is situated within the United States. The tax shall not apply to a transfer made on or before the date of the enactment of this Act.

"(c) The tax shall not apply to a transfer of property in trust where the power to revest in the donor title to such property is vested in the donor, either alone or in conjunction with any person not having a substantial adverse interest in the disposition of such property or the income therefrom, but the relinquishment or termination of such power (other than by the donor's death) shall be considered to be a transfer by the donor by gift of the property subject to such power, and any payment of the income therefrom to a beneficiary other than the donor shall be considered to be a transfer by the donor of such income by gift."

Section 504 of the Revenue Act of 1932 (47 Stat. 247) provides as follows:

"(a) GENERAL DEFINITION.—The term "net gifts" means the total amount of gifts made during the calendar year, less the deductions provided in section 505.

"(b) GIFTS LESS THAN $5,000.—In the case of gifts (other than of future interests in property) made to any person by the donor during the calendar year, the first $5,000 of such gifts to such person shall not, for the purposes of subsection (a), be included in the total amount of gifts made during such year."

It was held by the Board of Tax Appeals in Seymour H. Knox v. Commissioner, 36 B. T. A. 630, that where the petitioner had created one trust for the benefit of two individuals he was entitled to but one exclusion, the trust being the person constituting the donee within the meaning of the statute. This decision was followed in Katherine S. Rheinstrom v. Commissioner, 37 B. T. A. 308, and was also
22 followed and the same rule announced in Edwin B. Cox v. Commissioner, 38 B. T. A. 865. In numerous other cases the Board of Tax Appeals consistently held that there could be but one $5,000 exclusion where there was but one trust indenture, no matter how many donees might be named in each trust indenture.

Recently, however, the Board in the case of Wilton Rubinstein v. Commissioner, decided January 30, 1940, reversed its position and held where property was conveyed to a trustee for the benefit of the donor's wife and three children that four exclusions of $5,000 each should be allowed, basing its decision on Welch v. Davidson, 102 Fed. (2d) 100; Robertson v. Nee, 105 Fed. (2d) 651; Rheinstrom v. Commissioner, 105 Fed. (2d) 642; and McBrier v. Commissioner, — Fed. (2d) —, (C. C. A., 3d Cir., Dec. 19, 1939), P. H. 1939, ¶ 5.756.

Welch v. Davidson, supra, was an appeal from the judgment of the federal District Court of Massachusetts, in which judgment was awarded plaintiff for gift taxes paid by the plaintiff for the calendar year 1934. In 1934 the plaintiff and his wife created an irrevocable

trust, naming the Old Colony Trust Company as trustee, in which plaintiff transferred certain property for the benefit of his seven children. The instrument provides that upon plaintiff's death the proceeds are to be divided in equal shares, one for each of the seven children of the plaintiff then surviving, and one share for the issue of any child who has died, leaving issue. The trustee is to pay the income of each share to the child for whom it is held for life, paying one-half of the principal when said child reaches the age of 45, provided that at least ten years have elapsed after the plaintiff's death. The final date of distribution is set at 21 years after the death of the survivor of the plaintiff's children and grandchildren living at the time of the establishment of the trust. The District Court, Davidson v. Welch, 22 Fed. Supp. 726, held that the donor's seven children each took a one-seventh present interest in the res of the trust created, and that the donor was entitled to a $5,000 exclusion in respect to each of them. The judgment of the District Court was affirmed.

In Rheinstrom v. Commissioner, 105 Fed. (2d) 642, the taxpayer transferred personal property to trustees for the benefit of herself and her four children. By the terms of the trust instrument
23 she retained a life interest in 40% of the entire net income.
The trustees were directed to pay to her son, Stewart H. Clifford 12½% of the entire net income. They were directed to hold 12½% of such income for the benefit of her son Benjamin B. Clifford, but with the discretion to pay over to him only so much thereof as might to them seem best, and with power to pay all or a portion thereof to his wife "and/or" children; any unexpended portion of such income to be invested for his benefit "and/or" that of his wife and children. The trustees were directed to hold 12½% of such income for the benefit of the taxpayer's son, Arthur F. Clifford, upon the same terms and conditions as were applicable to Benjamin B. Clifford. The trustees were directed to hold 12½% of such income for the benefit of the taxpayer's daughter, Katherine Clifford, with discretion to pay over only so much of the income to her as to them seemed best, and to invest any unexpended balance for her benefit. The remaining 10% of the net income was to be accumulated, invested, and held "as a reserve fund, with absolute power and discretion in said trustees to pay over to" the taxpayer "during her lifetime, such part, if any, of this 10% of the entire net income of said trust, and accumulations, if any, thereon, as may to said trustees seem best, and with absolute power and discretion in said trustees, after the death of" the taxpayer, "to pay over to the children of" the taxpayer, "or to their successors in interest as hereinafter provided, such part, if any, of this 10% of the entire net income of said trust and accumulations, if any, thereon, as may to said trustees seem best. * * *"

In her gift-tax return for the year 1934 the taxpayer excluded $20,000 by virtue of Sec. 504 (b) on the theory that she had made four gifts in creating the trust, one to each of her children, and paid her taxes upon that basis. The Commissioner of Internal Revenue,

in auditing the return, determined that the taxpayer was entitled to but one $5,000 exclusion and asserted a deficiency. The Board of Tax Appeals sustained the Commissioner's determination and in its opinion, Katherine S. Rheinstrom v. Commissioner, 37 B. T. A. 308, 312, said:

"In this case there was a gift of one corpus to one trust by virtue of one trust instrument. Although there were four benefi-
24 ciaries, there was but one transfer made by the petitioner, which was to the trust itself. We must, therefore, conclude on the authority of previous decisions that but one gift was made, and only $5,000 may be excluded."

The court, insofar as here material stated the issue as follows:

"1. Did the transfer in trust constitute one gift to the trust or four gifts to the beneficiaries?

"2. If it constituted four gifts, were three of them gifts of 'future interests'?"

After a thorough consideration and discussion of the cases cited by both the plaintiff and the defendant, the court said, p. 647:

"It is our conclusion that the taxpayer, in creating this trust, made four gifts—one to each of her children—and that she made no gift or gifts to the trust or to the trustees.

"2. The Commissioner contends, however, that, even if this is so, it would make no difference in the taxpayer's gift tax liability, since only her son Stewart received an unconditional present vested interest in his share of the income of the trust estate, and the interests of the other three children are to be regarded as 'future interests.' The Commissioner directs attention to the fact that by the terms of the trust instrument the trustees are not required to pay to these three children their proportion of the income, but may accumulate it for their benefit, or, in the case of two of them, may pay it to them, their wives or children. It is true that the three children, other than Stewart, received no unconditional right to have their shares of the income paid to them by the trustees. It is equally true, however, that the taxpayer retained no interest in the shares of income which were assigned to them, and that, by the terms of the trust, each of them (or the wives and children of the two sons) were to have his or her share or it was to be accumulated for his or her benefit. The enjoyment of the benefits conferred upon three of her children by the taxpayer was conditional, but it was to commence at once and not at some future date and was for their sole and immediate benefit.

* * * * * * *

"The Commissioner cites no case which sustains his position that the interests donated by the taxpayer to, or for the benefit of, three of her children, were future interests, and we think that they were not.

* * * * * * *

25 "The decision of the Board is affirmed insofar as it holds that the taxpayer retained a life interest in only 40 percent of the income from the trust estate. It is reversed insofar as it holds that

the taxpayer was entitled to one exclusion for one gift, instead of four exclusions for four gifts. The case is remanded to the Board for a redetermination of the deficiency in accordance with this opinion."

In Commissioner v. Wells, 88 Fed. (2d) 339, it was held that the beneficiary of a trust which provided for the accumulation of income until he became of age, when he was to receive the income until he was 30, or until the death of his mother, when he was to receive the corpus, was not a gift of future interest, mainly upon the ground that it was the interest transferred by the taxpayer, and not that received by the beneficiary, which determined whether the gift was of a present or a future interest.

In Commissioner v. Krebs, 90 Fed. (2d) 880, the court dealt with trusts which directed the trustees to use the income from the trust estate for the support, maintenance, benefit, and education of named beneficiaries until they were 25 years of age, the unexpended income to be then paid to them or their issue, appointees, or distributees. It was held that the gifts, whether regarded as being to the trust or to the beneficiaries, were not gifts of "future interests."

In Noyes v. Hassett, 20 Fed. Supp. 31, the District Court of Massachusetts ruled that under a trust which permitted the trustees to accumulate income for the beneficiaries and to pay it to them or their guardians, or for the use or benefit of the beneficiaries, with discretion in the trustees to determine what expenditures were for the use or benefit of the beneficiaries, the gifts were not of future interests.

Thus it appears from the decided cases that the courts have rejected the contentions made by the defendant in this case. It is therefore held:

(1) That the gifts set up by plaintiff in the two trusts involved were of present interests in the property transferred, and

(2) That each beneficiary named in the respective trust instruments is a donee within the provisions of section 504 (b) of the gift-
26 taxing statute of 1932, for each of whom plaintiff is entitled to an exclusion of $5,000 in the computation of the net amount of gifts subject to the tax in each of the years involved.

Plaintiff is entitled to recover. The entry of judgment, however, will be suspended pending the filing of a stipulation by the parties showing the exact amount of the judgment to be awarded plaintiff, computed in accordance with the opinion of the court. It is so ordered.

WHITAKER, Judge; GREEN, Judge; and WHALEY, Chief Justice, concur.

LITTLETON, Judge, took no part in the decision of this case.

28 *V. Judgment*

At a Court of Claims held in the City of Washington on June 3, 1940, the court filed the following order entering judgment for plaintiff:

This case comes before the court on plaintiff's motion for the entry of judgment in accordance with the stipulation of the parties filed herein April 22, 1940, in which stipulation certain sums are mentioned as due plaintiff based on the special findings and opinion of the court filed March 4, 1940; and in accordance with said stipulation it is ordered this 3rd day of June 1940, that the plaintiff's motion for the entry of judgment be and the same is allowed, and judgment is now entered in favor of plaintiff in the sum of ten thousand, seven hundred twenty-seven dollars and one cent ($10,727.01), $317.43, a part thereof, to bear interest at the rate of six percent per annum from November 27, 1935; $6,265.83, a part thereof, to bear interest at the rate of six percent per annum from March 17, 1936, and the balance thereof, $4,143.75, to bear interest at the rate of six percent per annum from March 24, 1936, all according to law.

30 [Clerk's certificate to foregoing transcript omitted in printing.]

[Endorsement on cover:] Enter Attorney General. File No. 44742. Court of Claims. Term No. 393. The United States, Petitioner, vs. Arthur Pelzer. Petition for writ of certiorari and exhibit thereto. Filed September 3, 1940. Term No. 393 O. T. 1940.

U. S. GOVERNMENT PRINTING OFFICE: 1940

BLANK PAGE

Supreme Court of the United States

Order allowing certiorari

Filed October 21, 1940

The petition herein for a writ of certiorari to the Court of Claims is granted. And it is further ordered that the duly certified copy of the transcript of the proceedings below which accompanied the petition shall be treated as though filed in response to such writ.

281619—40

U. S. GOVERNMENT PRINTING OFFICE: 1940